Index-fund investors have options other than S&P 500

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Abstract:
Look for some less widely known index investments that track other indicators -- slices of the S&P 500 or the high-flying Nasdaq, for instance, or such specialized indexes as the ones that follow stock-car stocks or Internet companies.

Index investors fly on autopilot, buying mutual funds or other baskets of securities designed to mimic the performance of common market indicators like the S&P 500. Investors, thus, don't have to worry that their fund manager will lose his stock-picking touch, quit or fall under a bus.

Indexing is cost-efficient, with annual fees on good ones totaling 0.2 percent of assets or less, compared with about 1.5 percent for actively managed funds that must support analysts hunting hot stocks. Index funds are also tax-efficient. By forgoing the constant turnover of investments typical in managed funds, they escape most of the annual capital-gains taxes on profits that undermine managed-fund performance.

Full Text:

With the Standard & Poor's 500 off 5.05 percent this year, what's the dedicated index-style investor to do?

Look for some less widely known index investments that track other indicators -- slices of the S&P 500 or the high-flying Nasdaq, for instance, or such specialized indexes as the ones that follow stock-car stocks or Internet companies.

But first decide whether you want to pile onto a big winner, such as the pricey Nasdaq 100, up 25.51 percent this year, or bottom-fish out-of-favor issues such as aluminum, paper, steel and other basic-industry stocks that have been pummeled by their Old Economy reputations.

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If these benefits of indexing are not enough, the S&P 500 indexers also had a fabulous run in the 1990s, outperforming most actively managed funds on both a pre-and after-tax basis. Indexing was an easy investment choice when the S&P 500 was a winner.

But the S&P, which is dominated by big-company stocks, isn't shining as brightly these days. S&P 500 funds were down 4.47 percent from Dec. 31 through March 9, while the average diversified stock fund was up nearly 7 percent, according to Lipper Inc. Funds investing in small and midsize growth companies were up 34.14 percent and 33.25 percent respectively.

So what do you do if the S&P 500 turns you off but you still want the low fees, tax efficiency and other benefits of indexing?

You might start by looking at a variety of index products traded on the American Stock Exchange.

Each security represents a basket of issues that is traded like one stock. The disadvantage is that you have to pay a broker's commission to buy and sell, which you don't have with a no-load index fund. But that is not a serious problem if you use a cheap discount broker to invest a lump sum rather than making a series of weekly or monthly purchases.

One of the great high-fliers this year is the Nasdaq 100 tracking stock, which represents ownership of the 100 largest nonfinancial companies trading on the Nasdaq Stock Market. Traded under the symbol QQQ, it is up about 127 percent in the last 12 months.

Also doing well is the MidCap SPDR, which tracks the S&P 400 index of midsize companies (the ticker symbol is MDY). It is up 10.17 percent this year.

Then there are nine products called **Select Sector SPDRs**, each representing a subset of the S&P 500. These are most appealing right now to investors looking for beaten-down stocks that may represent bargains.

The basic industries basket (ticker: XLB) is composed of traditional manufacturers such as DuPont, Alcoa and Dow Chemical, and it is down the most, about 23 percent.

Other possible bargains: the cyclical/transportation basket (XLY), composed of companies such as Wal-Mart, Home Depot and Ford, off 19.6 percent; the financial basket (XLF), with stocks like Citigroup, American International Group and Bank of America, down 15.65 percent.

The big winner is the technology basket (XLK), composed of companies such as Microsoft, Cisco and Intel. It is up 10.9 percent.

Index investors looking for alternatives to the S&P 500 also should look at the scores of mutual funds that track U.S. and foreign stock indexes of small, medium and large companies as well as those focusing on specific industries.
